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Asian Crisis Redux: The Japanese Recession and a Devalued ¥en's Effects on Grain Trade

Summary

The first Japanese recession in 23 years, coupled with the recent tumble in the value of the yen will likely result in a marginal decrease in feedgrain imports. Furthermore, a faltering yen puts additional pressure on the Chinese currency (renminbi), which has stayed firm during the Asian financial crisis. A decrease in the renminbi's value would likely spark an additional round of Asian currency devaluations, impacting feedgrain demand throughout the region. However, a weaker yen can help boost Japan's economy, which is crucial for a rebound in Asian feedgrain demand.

Changes in Japanese Demand: Not Dramatic, but Noticeable

One of the likely effects of the recession on Japan will be a marginal strengthening of rice and wheat product demand, as people reduce consumption of meat and animal products. While imports of feedgrains by Japan thus far in 1998 are moving along at a pace unchanged from the past several years, there are signals that this may not continue:

- Compound feed production has fallen marginally;
- Sales of compound feed to feedlots are nearly 6 percent below last years' level;
- Inventories of compound feed have risen over the past several months to levels nearly 30 percent higher than this time last year;
- The dairy, livestock, and poultry herds are shrinking; the swine sector is not growing.

Of these factors, perhaps the strongest indication of future slackening of import demand is the increase in compound feed inventories. This sends a very clear signal to feed compounders not to continue purchasing corn at the present pace, particularly as the faltering yen makes imports more expensive, and large stockpiles depress compound feed prices.

The Ripple Effect of the Devalued Yen

As Japan is by far the largest trading partner with Southeast Asia, and over one-quarter of China's foreign exchange reserves are denominated in yen, the value of the yen will have far-reaching effects on Asian economies and their demand for grain imports.

Southeast Asia:

Prospects for a rebound in feedgrain imports by this region hinge on the ability of these economies to return to positive economic growth. The primary destination of Southeast

Asia's exports (agricultural and other) is Japan. The weaker the yen, the less competitive these exports, thus dampening the efforts of many of these countries to "export themselves out of a crisis". Furthermore, a volatile yen impacts efforts by regional financial institutions to recapitalize after the setbacks suffered over the past year.

China:

Regardless of the yen's value, demand for feed in China is expected to continue to show sluggish growth, enabling China to continue corn exports. Economic growth is likely to slow because of increased trade competition coming from the devaluation of other Asian currencies, and because of reduced capital inflows. In addition, these reduced inflows are likely to reduce job creation in the non-state sector, hence making state-owned enterprise restructuring more difficult. This will pressure the Chinese government to keep grain support prices at high levels, to minimize population migration to urban areas, where unemployment is already at high levels. The result will be probable increases in already-burdensome grain stockpiles, not only of corn, but wheat and rice as well. This situation could only be worsened by continued devaluation of the yen.

The Outlook...

The near-term effects of the current situation will be for slackened feedgrain import demand, both in Japan and the rest of Asia. Global grain prices could also suffer. However, the more quickly the Japanese economy recovers, the sooner feedgrain demand in Asia will rebound, and a weaker yen could forestall a prolonged Japanese recession. However, it is crucial that the yen not fall too far, sparking another round of devaluations, denying the Japanese economy the benefits of a softer yen. A too-weak yen could also create a "credit crunch" in under-capitalized Japanese banks that could spread throughout Asia.

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